

A nonprofit organization may qualify for exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954 where it obtains funds for charitable grants and contributions through acquisition, with borrowed money, of oil and gas production payments.

Advice has been requested whether under the circumstances described below an organization may qualify for exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954.

An organization organized exclusively for charitable purposes obtains funds for its operations principally through the acquisition, with borrowed money, of oil and gas production payments. The excess of the so-called interest equivalent factor paid in connection with each oil production payment over the interest rate charged by the lender of the borrowed funds, a spread generally averaging between one-quarter and one-half of 1 percent on each production payment purchased, provides the funds for the organization's charitable program. The organization carries out its charitable purposes by contributing to other qualified charitable organizations.

The courts have uniformly held that the purchase of oil production payments in the manner described by an organization otherwise qualified for exemption from Federal income tax under section 501(a) of the Code does not constitute the conduct of trade or business for profit and has held that engaging in such transactions does not affect the organization's exempt status. See *Bright Star Foundation v. Campbell*, 191 F.Supp. 845 (1960); *Southwest Endowment Corp. v. U.S.*, 1. A.F.T.R.2d 1869, 58-2 U.S.T.C. 9577; *First Dalls Charitable Corp. v. U.S.*, 11 A.F.T.R.2d 312, 63-1, U.S.T.C. 9117; *Southwest Charitable Corp. v. U.S.*, 11 A.F.T.R.2d 313, 63-1 U.S.T.C. 9118; *B.G.S. Foundation v. U.S.*, 11 A.F.T.R.2d 314, 63-1 U.S.T.C. 9116; and *Foree Foundation v. U.S.*, 11 A.F.T.R.2d 314, 63-1 U.S.T.C. 9115.

The Service will follow the decisions in the cited cases. Accordingly, the subject organization is exempt from Federal income tax under section 501(c)(3) of the Code. See Revenue Ruling 66-295, page 207, this Bulletin, which holds that an organization obtaining its income in a similar manner is exempt from Federal income tax under section 501(c)(2) of the Code.

An organization which considers itself within the scope of this Revenue Ruling must, in order to establish exemption under section 501(c)(3) of the Code, file an application on Form 1023, Exemption Application, with the District Director of Internal Revenue for the internal revenue district in which is located the principal place of business or the principal office of the organization. See section 1.501(a)-1 of the Income Tax Regulations.